

503-236-5638

IN REPLY
REFER TO:

United States Department of the Interior

BUREAU OF RECLAMATION
Pacific Northwest Region
1150 North Curtis Road, Suite 100
Boise, Idaho 83706-1234PN-3324 -
WTR-4.00

MAY 17 2000

MEMORANDUM

To: Commissioner
Attention: W-1000From: J. William McDonald
Regional Director, Boise IDSubject: Cost Reallocation Interim Report, Columbia Basin Project, Washington

Attached for your consideration and approval is the subject report titled "Interim Cost Reallocation Report, Columbia Basin Project, Washington, May, 2000."

Previous Allocations: The original allocation of costs for the Columbia Basin Project (Project) was prepared in 1945 and printed as House Document 172, 79th Congress.

In 1963, a revised allocation was prepared and approved, titled "Interim Report, Allocation of Costs, Columbia Basin Project, Washington, January, 1963." The percentages developed in the 1963 allocation for allocating capital costs of joint use project facilities to irrigation, power, and flood control are those used in the current Project financial statements and for assigning certain reimbursable operation and maintenance (O&M) costs to project functions.

Background, Current Reallocation: The Project has undergone considerable change since 1963. The major changes being (1) the Third Powerplant was authorized in 1966 and subsequently constructed; (2) pump units 7-12 were approved and converted to pump-generating units; (3) construction appropriation requests for development of the second half of the irrigation project are no longer included in budget documents—although not deauthorized; and (4) the Project is now operated to accommodate additional power considerations, resource needs on the Project, and Endangered Species Act and other needs of the coordinated Columbia River operating system.

In 1995, the Office of the Inspector General completed an Audit Report on the Recovery of Construction Costs; Columbia Basin Project. The audit included a recommendation that:

"To correct this deficiency, we recommend that the Bureau prepare an interim cost allocation for the Project that reflects the Project as currently constructed, with an assumption that additional irrigation acreage will not be developed. Upon completion, this allocation should be submitted to the Congress for approval before it is actually implemented."

A July 6, 1995, letter from the Acting Commissioner to the Office of Inspector General concurred with their recommendation:

"Reclamation will revise the interim cost allocation which reflects the Columbia Basin Project as currently constructed and will assume that additional irrigated acreage will not be developed. The appropriate review and approval process will be followed prior to implementing the interim cost allocation."

Current Reallocation Results: The allocation was completed using the Alternative Justifiable Expenditure method, the same method used in the 1945 and 1963 allocation reports. The total construction cost subject to reallocation is \$1,702,387,050. An additional, approximately \$7.1 million is directly assigned or has special legislative disposition.

The proposed reallocation now includes a municipal and industrial (M&I) function as part of a "water supply" function which includes irrigation. Functions sharing in the distribution of joint project costs are irrigation, M&I water supply, power, and flood control. Upon advice from the Corps of Engineers, the navigation function is no longer applicable, and no allocation was made to navigation.

The essential changes in the proposed reallocation of construction costs from the 1963 allocation as currently applied on Project financial statements are (1) an increase in costs allocated to commercial power, (2) a decrease in costs allocated to irrigation and flood control, (3) elimination of the navigation function, and (4) the addition of M&I as a project function. In accordance with House Document 172, the reallocation also results in commercial power picking up a greater share of the O&M cost of Grand Coulee Dam and Reservoir--from 69.87 percent to 92.054 percent.

Shown below is the proposed allocation of Project construction costs by function, including a comparison with the 1963 allocation and the allocation in the fiscal year 1999 Project Cost and Repayment Statement. The proposed allocation costs will be reconciled with the actual cost to date.

Function	1963 Interim Allocation		FY 1999 Statement of Project Construction Cost and Repayment		Proposed Reallocation	
	Percent Distribution of Joint Cost	Amount (dollars)	Percent Distribution of Joint Cost	Amount (dollars)	Percent Distribution of Joint Cost	Amount (dollars)
Water Supply Irrigation M&I	27.4 NA	738,325,000 0	27.4 NA	667,784,188 0	12.39 (12.344) (.046)	543,948,761 1,984,232
Power (commercial)	43.1	172,582,000	43.1	996,731,976	79.71	1,129,541,983
Flood Control	29.5	48,798,000	29.5	52,104,510	7.9	26,912,074
Navigation	-	1,000,000	-	1,000,000	0	0
Other	-	499,000	-	0	-	0
Subtotal	100.00	961,204,000	100.00	1,717,620,674	100.0	1,702,387,050
Adjustments/Other		-		30,706,573		7,113,916
TOTAL		961,204,000		1,748,327,247		1,709,500,966

Repayment Considerations: Repayment of allocated costs is in accordance with Reclamation law and the Columbia Basin Project authorization. Functional repayment requirements are as follows.

Construction costs allocated to irrigation are reimbursable without interest. As the obligation of district irrigators is essentially fixed by contract, the decrease in the allocation to irrigation will be accommodated by a reduction in the amount of financial assistance to irrigation, as authorized, from the Federal Columbia River Power System (FCRPS).

Construction costs allocated to M&I, including interest during construction, are reimbursable with interest and will be returned through rates established in M&I contracts.

Costs allocated to flood control are nonreimbursable.

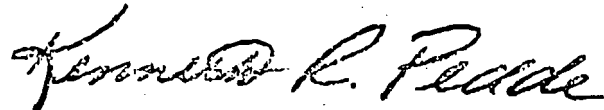
Construction costs allocated to commercial power, including interest during construction, are reimbursable with interest by the FCRPS as administered by the Bonneville Power Administration (BPA).

The reallocation also results in an increase in the share of O&M costs of Grand Coulee Dam and Reservoir, from 69.87 percent to 92.054 percent, that is payable by the BPA.

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Implementation: The costs allocated to commercial power are recovered through power rates established by the BPA for various classes of customers. BPA has recently completed the rate establishment process for the "2002 Power Rate Case," which establishes power rates for the period October 2001 through September 2006. The 2002 Power Rate Case is predicated on existing and projected future debt service and operating costs requirements. Because the incremental debt service amounts associated with the proposed reallocation were not anticipated in that process, BPA has asked Reclamation that the reallocation not be implemented until the end of the 2002 Power Rate Case period (i.e., September 30, 2006). At that time, BPA will have had the opportunity to include such costs in its post-2006 rates. I agree with BPA's reasons for the delay and hereby request that the implementation of the reallocation in the Project's financial statements and records not take place until fiscal year 2007.

I recommend that you approve the interim reallocation report as set forth in the attached document.



Attachment

cc: Ms. Judi Johansen
Administrator
Bonneville Power Administration
PO Box 3621
Portland OR 97208-3621

Director, Office of Policy
Attention: W-5000, D-5200
Director, Operations
Attention: W-6000, W-6331, W-6300
Director, Technical Service Center
Attention: D-8270
(each w/att)

bc: W-6331 (w/att)

WBR:ARainers:ko:5/12/00 (208)378-5344
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6/1/00 Copy to PN-1820 (Michelle Z.)



United States Department of the Interior

BUREAU OF RECLAMATION
Washington, D.C. 20240

IN REPLY REFER TO:
D-5200

JUL 10 2000

MEMORANDUM

To: Regional Director, Boise, Idaho
Attention: PN-1000

From: Eluid L. Martinez
Commissioner

Subject: Approval Memorandum for Cost Reallocation Interim Report, Columbia Basin Project, Washington

This is in response to your memorandum of May 17, 2000, in which you requested approval of the subject report entitled "Interim Cost Reallocation Report, Columbia Basin Project, Washington, May 2000." This cost reallocation is considered "interim" because the project has not been completed. The original authorization has not been amended and remains in place.

The principal purposes of a cost allocation are to assign specific and separable costs to individual project purposes and to determine an equitable allocation of the remaining joint costs to those same authorized project purposes. Several methodologies are available to perform the allocation, including the alternative justifiable expenditure (AJE) method. This method was used for the allocations completed in 1945 and 1963, and for consistency and because it appeared to be appropriate, this method was used in the subject interim allocation as well.

The last interim allocation of costs was completed in 1963, and significant changes have occurred since then that would influence the allocation of the project investment costs. The 1963 analysis preceded the addition of the third powerplant and pump-generating units and also assumed development of the full 1,029,000 acres for irrigation. The subject interim allocation utilized only the 671,000 acres that are currently in service. These specific changes along with the recommendation from the Office of Inspector General (OIG) resulted in a decision to perform a new interim allocation of project investment costs. In part, the recommendation of the OIG states "that the Commissioner, Bureau of Reclamation, ensure that the Pacific Northwest Region prepares an interim cost allocation for the Columbia Basin Project that reflects the Project as currently developed."

Rather than allocate directly to irrigation in this allocation, costs were first allocated to the water supply purposes. These costs were then further suballocated to irrigation, and municipal and industrial (M&I) water supply. This procedure permitted costs to be allocated to M&I, which had not been done in previous allocations. It should be noted that M&I service is not specifically

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identified as a project purpose in the authorizing legislation, but allocating costs to this purpose will allow these costs to be recovered through existing or future M&I contracts. Costs allocated to power were also suballocated with a portion of the costs being allocated back to irrigation, since part of the power production is used to pump water for this purpose.

Flood control is an authorized project purpose; however, estimates of flood control benefits attributable to project facilities were reduced in absolute and relative terms compared to the previous allocations. This occurs because of additional storage constructed elsewhere in the basin and the addition of levees downstream from the project. Navigation was initially considered to be a project purpose with benefits attributed to the reduction in the cost of annual maintenance dredging. The Corps of Engineers has now found the benefits derived from the facilities to be minimal due to downstream channel deepening, construction of upstream dams, and the use of pile dikes in the lower reaches of the river to train the river flows. Thus, no costs have been allocated to this purpose.

These changes in assumptions and computational procedures resulted in the following proposed interim allocation contained in the subject report. This allocation is compared here to the 1963 allocation for background purposes.

	<u>1963 allocation</u>	<u>Proposed allocation</u>
Power	\$172,582,000	\$1,129,541,983
Irrigation	738,325,000	543,948,761
M&I	-	1,984,232
Flood control	48,798,000	26,912,074
Navigation	1,000,000	-
Other	499,000	-
Total	\$961,204,000	\$1,702,387,050

The subject interim reallocation report is approved with the following understandings:

1. The interim reallocation will be put into effect on October 1, 2000, and will not be applied retroactively (i.e., it will not apply to past payments made by the Bonneville Power Administration (BPA) pursuant to the 1963 interim reallocation report).

2. The reallocation results in an increase in reimbursable investment costs allocated to commercial power. The repayment of such costs is the responsibility of the Federal Columbia River Power System (FCRPS). The payment of the investment will be in accordance with the Project authorizations and BPA's payment priority under applicable authority for repaying FCRPS costs and its associated agreements with Treasury.

3. Interest will accumulate on any unpaid investment. In other words, interest will begin accruing on the interest bearing components of the interim reallocation beginning on October 1, 2000, at the appropriate authorized project interest rates or other rates applicable to

FCRPS costs. However, it is recognized that BPA may choose from among several methods to repay the commercial power investment obligation to the U.S. Treasury within the prescribed 50-year period, including lump sum, periodic payments, or deferred payments.

4. The interim reallocation includes allocations to flood control and to water supply which, in turn, was suballocated to irrigation and M&I. Allocations to these purposes will also be implemented October 1, 2000. As the irrigation repayment and water service contracts specify fixed obligations, the irrigation assistance from the FCRPS will be adjusted accordingly. Investment cost allocated to M&I will be recovered via existing and future M&I contracts.

5. The new allocation for operations and maintenance (O&M) will be implemented on October 1, 2000. This will increase the proportion of Grand Coulee Dam and Reservoir O&M costs paid by BPA from 69.87 % to 92.054 %. However, I understand that there will be no impact to the O&M costs which the project irrigation districts pay since these costs are established under a separate process. Under this process, Reclamation recovers irrigation O&M costs through a 5-year, fixed-rate per acre-foot charge for water delivered to the irrigation districts which charge is established by criteria in article 36 of the December 1968 arrendatory contracts, i.e., the Diversion Rate. A new irrigation O&M rate was recently established for the period 2000-2004 with the execution of a Diversion Rate agreement.

If you have any questions, please contact Larry Schluntz at 303-445-2901 or via the LAN.